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PROCUREMENT STRATEGY ROLE IN THE PERFORMANCE OF PUBLIC LIMITED AND PRIVATE LIMITED COMPANIES

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ABSTRACT

The paper presents a study relating to the strategic decision of make or buy, type of companys incorporated and organizational performance. A study was conducted on manufacturing companys in Malaysia. Convenience sampling was done and 314 companies responded in this study. The findings indicate that there were no significant differences between the performance of companies that 'make' or 'buy'. But when the two groups were further scrutinised, based on the type of company incorporated, the results indicated the companys incorporated as 'public limited company' perform better than the 'private limited company'. However, the combination of type of company incorporated (public limited company – big company, and private limited company – medium size company) with procurement strategy does effects organizational performance. This study found, private limited companies that opted for make strategy perform better than other type of combinations. This means, the type of companys incorporated is an important indicator in determining the most appropriate procurement strategy, which positively related to performance, and could enhance competitiveness of a company in facing today's hyper competitive environments. The findings may add another dimension for consideration in the strategic decision choice process.

Field of Research: Procurement, Make-Buy Strategy, Type of Corporation, Performance

INTRODUCTION

Over the past decade there is a growing realisation of the important contribution of purchasing and supply (Cousins, Lawson, & Squire, 2006) to company's performance. This study focused on procurement strategy in lieu to the developments of its practices which has become an important factor for companies' competitive advantage (Kemppainen & Vepsalainen, 2003), and a key factor in enhancing companies' performances (Lee & Billington, 1992; McIvor, 2000; Bovet & Martha, 2003). Both academicians and practitioners confirmed that effective procurement strategy would lead to sustainable competitive advantage. With globalization correct procurement practices, it has become an important factor in managing operations (Carter, Monckza, & Slaight, 2000).

In general, an effective procurement strategy has the ability to (a) decide between make versus buy decision based on transaction cost theory (Walker, 1988; Venkatesan, 1992; Sisilan

& Satir, 2000), (b) integrate procurement strategies with company strategies (Freeman & Cavinato, 1990), (c) convert fixed costs into variable costs (Welch & Nayak, 1992), (d) deliberate reduction of vertical integration (Hill, 1994), (e) determine the total cost ownership and purchasing strategy (Anderson & Katz, 1998), (f) develop the process of designing and managing supply networks in line with operational and organizational performance objectives (Narasimhan & Das 1999), and (g) plan, evaluate, implement, and control the procurement decisions (Carr & Smeltzer, 1997; Carr & Pearson, 2002).

Basically, previous research on procurement strategy can be classified into two groups: (a) focus on the make versus buy decision that concentrates on issue such as whether or not in-house production provides the company with competitive advantage (Handfield, Krause, Scannell, & Monczka, 2000; Sislian & Satir 2000); and (b) focus on the issue of whether or not companies have the capabilities to produce in-house.

It is a question on whether or not a company is competent to retain its operations or should it acquires the needed capabilities or should it establish partnership with suppliers to outperform competition (Walker 1988; Anderson & Katz 1998; Sislian & Satir 2000). Research on this issue is also centred on the long-term implications of procurement for the procurement process and buyer-supplier relationships (Anderson & Katz 1998; Narasimhan & Das 1999; Sislian & Satir 2000). The objectives of this paper are to examine the procurement practices (make or buy), the effect of the procurement decision, and the type of companies incorporated and its effect on organizational performance in the context of manufacturing companies in Malaysia.

LITERATURE REVIEW

The literature shows many companies are obviously working hard toward achieving objectives like cost reduction, quality, service and delivery improvement, organizational focus, flexibility enhancement and change facilitation (Fan, 2000; Zeng, 2000; Humphreys, Low & McIvor, 2000; Canez, Platts, & Probert, 2000; Jennings, 2002; Gilbert, Xia, & Yu, 2006).

Unfortunately, most of them are still using the conventional approach that is on a short-term basis where the result of such approach is known to be discouraging (Narasimhan & Das 1999; Sislian & Satir 2000). Leading-edge multinationals company already recognize the fallacy of this approach as they realize the competition in not on a short-term basis (fire fighting) but rather it's on a long-term basis (strategic) (Narasimhan & Das 1999; Sislian & Satir 2000).

One of the key issues of procurement strategy in manufacturing industry is the growing importance of the make or buy decision. Surveys have shown that senior managers in manufacturing industry are unanimous in their view that such decision should be part of their business strategy (Probert, 1996). Traditionally, buying by organizations has been done largely on the basis of obtaining the best price, exceptionally taking into account a few other factors such as quality and delivery.

Few have treated this make or buy decision as a strategic issue, with many companies deciding to buy rather than make for short-term reasons of cost reduction (Ford, Farmer, Gross, & Wilkinson, 1993). Historical events, such as the 1970s Arab-oil embargo in the USA, had caused companies to recognize the strategic role of procurement and turned the make or buy practices from a low skilled clerical function to a highly skilled strategic function where they

are involved in strategic decisions and managing the company's procurement decisions (Ellram & Carr, 1994).

The recognition is even more now as many leading companies have considered the control of costs and supply management as important factors in maintaining the ability to remain competitive (Carr, Monczka, & Slaight, 2000; Cousins, 2005). The theory behind the conceptual basis for the procurement decision is Williamson's (1975) theory of transaction cost analysis, and resource based view (RBV) (Penrose, 1959; Wernerfelt, 1984; Ettlie & Sethuraman, 2002).

If leading companies recognized the strategic role of procurement strategy, how do companies of different sizes perceived this issue and in relation with performance? This study classified companies into four categories: (a) private limited company (medium), (b) public limited company (large), (c) partnership (large/medium), and (d) sole proprietorship (small).

PROCUREMENT STRATEGY - MAKE

Lamming (1996) claimed that there could be no authentic, identifiable best practice in inter-organization relations due to difficulties to manage, or conceptualize the complex relationship between businesses organizations involved. This perhaps could be the main reason for the existence of different relationship types among the members of a supply chain (Spekman, 1988; Petterson, Frayer, Scannell, 1999; Wong, 1999; Forker & Stannack, 2000; Stuart & McCutcheon, 2000).

A company may opt for make strategy when external capabilities do not exist outside or even if they do exist, they cannot be traded through markets or across companies (Capron & Mitchell, 2004), or when suppliers do not want to trade unique and valuable resources (Dierickx & Cool, 1989). So, to remain competitive, companies need to develop the ability to recombine its internal capabilities into new configurations of capabilities (Henderson & Clark, 1990; Galunic & Rodan, 1998). This clearly indicates its strong association with related product diversification strategy (Grant, 1996; Simonin, 1999).

Capron and Mitchell (2004) also find, consistent with knowledge-based theorists, companies prefer make strategy than buy strategy when the targeted capabilities and the company's existing capabilities are narrow. Furthermore, consistent with the institutional theorists, they find that 'make' is more suitable than 'buy' strategy in developing capabilities that do not depart significantly from the company's routines and social values. In turn, they also find that some reconfiguration routines moderate the capability attributes. However, owing to rapid changes in the market, this strategy makes companies less flexible (Hayes & Abernathy, 1980).

PROCUREMENT STRATEGY – BUY

The strategy to 'buy' or outsourcing is an act of moving some of a company's internal activities and decision responsibilities to outside providers (Lankford & Parsa, 1999). Companies nowadays tend to contract out more manufacturing and service activities than they did a decade ago (Fuller, 2002). This trend has been driven by changes in the business environment and the pursuit of lean operations (Hui & Tsang, 2004).

The buy strategic option has enable companies to secure advantages such as economies of scale (mass production) and scope (specialization), cost reduction, quality, service and delivery improvement, organizational focus, product flexibility enhancement and exploit change facilitation provided by external suppliers (McIvor, Humphreys & McAleer, 1997; Fan, 2000; Zeng, 2000; Kakabadse & Kakabadse, 2000; Jennings, 2002; Hui & Tsang, 2004; Gilbert et al., 2006), as well as gain new knowledge or realised the need for additional product development resources to speed up the time taken to deliver to the market (Fan, 2000; Jenning, 2002; Barragan, Cappellino, Dempsey, Rothenberg, 2003).

The reason why OEM such as Alcatel adopt this trend is not so much to reduce costs, but because it gives them more flexibility to adapt to market changes. There is no doubt that buy strategy has strong relationship with product flexibility (Ghausi, 2002; Jennings, 2002), and unrelated product diversification (McCarthy & Anagnostou, 2004; Jin, 2004).

PROCUREMENT DECISION, TYPE OF COMPANY INCORPORATED AND PERFORMANCE

Globalization has turn the 'make' and 'buy' decision no longer tactical but a strategic issue (McIvor & Humphreys, 2000), and has become a major determinant of profit and a significant contribution to the financial health of the company (Yoon & Naadimuthu, 1994; McIvor & Humphreys, 2000; Zeng, 2000; Cousins *et al.*, 2006).

Meanwhile, the relationship between company size and performance has been the subject of many researches. Some findings support the positive relationships but some have provided conflicting results. A number of researches have indicated a positive relationship between company size and performance (Hall & Weiss, 1967; Demsetz, 1973; Scherer, 1973; Obaidat, 1987). However, others reported a negative relationship between them (Cubbin & Leech 1986; Dobson & Gerrard, 1989; Reid, 1995).

Hypotheses

The paper proposes three hypotheses and they are:

H1: There is a significant difference in the performance of companies that opted for make or buy strategy.

H2: There is a significant difference in the performance of companies that incorporated as private limited or public limited companies.

H3: There is a significant difference between the performances of public limited companies and private limited companies that opted for make or buy strategy.

METHODOLOGY AND RESEARCH DESIGN

The total numbers of respondents were 314, and were convenience sampled from the 2007 member list of the Federation of Malaysian Manufacturers (FMM). Questionnaires were mailed specifically to senior personnel in the procurement sector who would be able to respond comfortably to the issues studied. The instrument used by Kotabe and Omura (1989) on

procurement strategy was adapted. Twelve questions on various procurement practices were used.

For the organizational performance, seven questions that covered both financial and non financial measures were also taken and adapted from four different studies (Venkatraman & Ramanujam, 1986; Dess & Robinson, 1994; Lee & Miller, 1996; Kaplan & Norton, 1996). For the company type of incorporated, procurement pattern and source of supply, it was developed and validated through a focus group process.

FINDINGS AND DISCUSSIONS

H1: There is a Significant Difference in the Performance of Companies that opted for 'Make' or 'Buy' Strategy

Table 1
Group Statistics

	SSMB	*N*	*Mean*	*Std. Deviation*	*Std. Error Mean*
GP	1.00	153	5.8618	.40751	.03295
	2.00	161	5.8296	.46167	.03638

Table 2
Independent Sample Test

		Levene's Test for Equality of Variances		*t-test for Equality of Means*						
		F	*Sig.*	*t*	*df*	*Sig. (2-tailed)*	*Mean Difference*	*Std. Error Difference*	*95% Confidence Interval of the Difference*	
GP	Equal variances assumed	1.616	.205	.653	312	.514	.03218	.04924	-.06471	.12906
	Equal variances not assumed			.656	310.329	.513	.03218	.04908	-.06440	.12875

The above tables show the relevant statistical data on the two category of companies (high percentage of make=1; and buy=2). An independent sample t-test was conducted to compare the performance of those two groups. There was no significant difference in the scores for make ($\underline{M}$ = 5.86, $\underline{SD}$ = 0.42), and buy ($\underline{M}$ = 5.83, $\underline{SD}$ = 0.46); $\underline{t}$ = 0.65; $\underline{df}$ = 312, and $p > 0.05$. Thus, HI is rejected.

Discussion: The study indicated that the performances of companies were not influence by their decision whether to buy or make. Such decision though strategic do influence the performance but there is no indication that companies that buy perform better than those that make in the context of manufacturing companies in Malaysia.

H2: There is a Significant Difference between the Performances of Companies that Incorporated as Private Limited or Public Limited Company

Out of the four type of companies' mentioned, only two were involved this study: (a) private limited company (medium size company), and (b) public limited company (large size company). Tables 3 and 4 below illustrate the statistical analysis of the two group respondents.

Table 3
Group Statistics

	D2	*N*	*Mean*	*Std. Deviation*	*Std. Error Mean*
OP 1	Private Limited Company	275	5.8239	.42342	.02553
OP 2	Public Limitedcompany	39	5.9963	.49431	.07915

Out of 314 companies, the majority (275) of the companies were incorporated as private limited companies.

Table 4
Independent Sample Test

		Levene's Test for Equality of Variances		*t-test for Equality of Means*						
		F	*Sig.*	*t*	*Df*	*Sig. (2-tailed)*	*Mean Differ-ence*	*Std. Error Difference*	*95% Confidence Interval of the Difference*	
OP	Equal variances assumed	2.204	.139	-2.329	312	.020	-.17244	.07403	-.31811	-.02677
	Equal variances not assumed			-2.073	46.250	.044	-.17244	.08317	-.33983	-.00505

The above tables show the two category of companies (high percentage of private limited company =1; and public limited company=2). An independent sample t-test was conducted to compare the performance of the two categories of companies. There was significant difference in the scores for private limited company ($\underline{M}$ = 5.82, $\underline{SD}$ = 0.42), and public limited company ($\underline{M}$ = 6.00, $\underline{SD}$ = 0.49); t = -2.33; $\underline{df}$ = 312, and $p > 0.05$. Thus, H2 is supported.

Discussion: The study indicated that the performances of companies were influence by their type incorporated either as private limited or public limited companies. Specifically, public limited company performs better than private limited company in the context of manufacturing companies in Malaysia. This result confirms previous study findings which supported the size of a company size has a positive relationship with performance (Hall & Weiss, (1967; Demsetz, 1973; Scherer, 1973; Obaidat, 1987).

H3: There is a Significant Difference between the Performances of Public Limited and Private Limited Companies that opted for Make or Buy Strategy

Table 5
Data According to Category (Organizational Performance)

Group (SSD2)	*N*	*Mean*	*Std. Deviation*	*Std. Error*	*95% Confidence Interval for Mean*		*Minimum*	*Maximum*
1.00	129	5.8660	.38950	.03429	5.7981	5.9339	5.00	7.00
2.00	146	5.8611	.46736	.03868	5.7846	5.9375	5.00	7.00
3.00	24	5.8393	.50254	.10258	5.6271	6.0515	5.00	7.00
4.00	15	5.5238	.25133	.06489	5.3846	5.6630	5.14	5.86
Total	314	5.8453	.43573	.02459	5.7969	5.8937	5.00	7.00

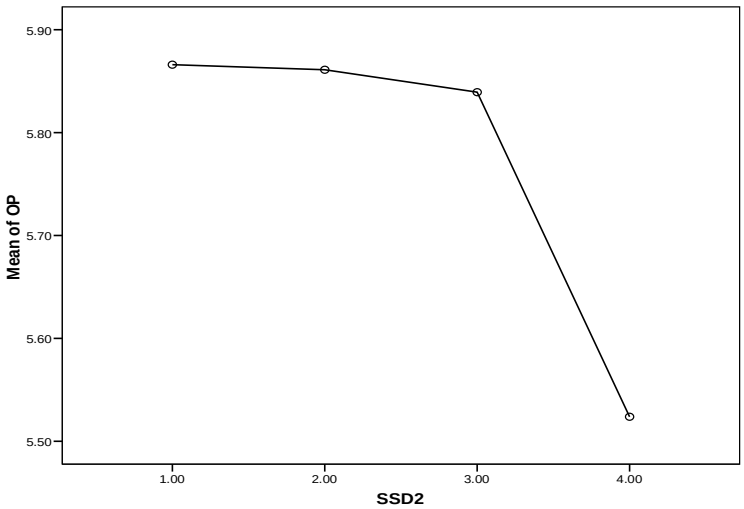
Group 1 = PLC + Make (Private-Make) Group 2 = PLC + Buy (Private-Buy)
Group 3 = Pub LC + Make (Public-Make) Group 4 = Pub LC + Buy (Public-Buy)

Table 5
ANOVA (Organizational Performance)

	Sum of Squares	*Df*	*Mean Square*	*F*	*Sig.*
Between Groups	1.643	3	.548	2.938	.033
Within Groups	57.783	310	.186		
Total	59.425	313			

A one way ANOVA analysis between groups was done to explore the impact of type of company incorporated. There was significant difference at the $p < 0.05$ level in categorised scores for the four groups $F(3, 310) = 2.94$. Thus hypotheses H3 is supported. Despite indicating significant difference statistically, the actual differences in mean scores between the groups were quite small as illustrated in Chart 1 below.

Chart 1: Means Plot Organizational Performance (OP) vs. Group (SSD2)



Discussion: The means plot indicate that group 4 (public-Buy) that opted for buy strategy recorded the lowest organizational performance scores with the group 1 (Private-Make) which is private limited company that opted for make strategy recording the highest. Even though, the plot shows significant differences but actually it is not so as the scale used is small.

Table 6
Multiple Comparisons: Dependent Variable: OP

(I) SSD2	*(J) SSD2*	*Mean Difference (I-J)*	*Std. Error*	*Sig.*	*95% Confidence Interval*	
1.00	2.00	.00495	.05217	1.000	-.1298	.1397
	3.00	.02672	.09598	.992	-.2212	.2746
	4.00	.34219(*)	.11778	.020	.0380	.6464
2.00	1.00	-.00495	.05217	1.000	-.1397	.1298
	3.00	.02177	.09510	.996	-.2239	.2674
	4.00	.33725(*)	.11706	.022	.0349	.6396
3.00	1.00	-.02672	.09598	.992	-.2746	.2212
	2.00	-.02177	.09510	.996	-.2674	.2239
	4.00	.31548	.14210	.120	-.0516	.6825
4.00	1.00	-.34219(*)	.11778	.020	-.6464	-.0380
	2.00	-.33725(*)	.11706	.022	-.6396	-.0349
	3.00	-.31548	.14210	.120	-.6825	.0516

* The mean difference is significant at the .05 level.

Even though the performance of both private limited and public limited companies were significant but their level of significance were not differ much form one another. Specifically, the results presented in Table 6 as above, only three groups; Group 1 (private-make), Group 2 (private-buy), and Group 4 (public-buy) are statistically significantly different from one another but the differences were very small.

CONCLUSION

This study on the competitiveness of manufacturing companies in Malaysia focussed on the procurement decisions, which has been recognised as importance in strategic decision making process. However, the study, clearly distinguished the make or buy strategies had significant impact on performance. The general perception that buy (outsourcing) would result in better performance does not stick.

The type of companies incorporated that is private limited, and public limited companies had impact on performance. The results show that public limited perform better than the private limited companies. This means the types (size) of companies do have positive relationship with performance.

Furthermore, the private limited companies with make procurement strategy perform slightly better than other groups. The least effective combination was the public limited company that adapted the buy strategy. However, their differences from one another were not so significant.

With the current trend of globalisation, the findings of this study would help managers to determine the best procurement strategy for their products. Further research on procurement

strategy is needed especially in determining its actual benefits especially for the small and medium enterprises which have yet to be laid down clearly. The move towards clustering production facilities could also be another dimension to add.

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